US SIF

The Forum for Sustainable and Responsible Investment

January 31, 2020

Ms. Vanessa A. Countryman, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-22-19

Dear Ms. Countryman:

US SIF: The Forum for Sustainable and Responsible Investment ("US SIF") is pleased to submit comments on the proposed rules described in *Amendments to Exemptions from the Proxy Rules for Proxy Voting Advice*, Release No. 34-87457, 84 Fed. Reg. 66418 (Dec. 4, 2019) (the "Release").

US SIF is the leading voice advancing sustainable, responsible and impact investing across all asset classes. Our mission is to rapidly shift investment practices toward sustainability, focusing on long-term investment and the generation of positive social and environmental impacts. Our members, comprised of investment management and advisory firms, mutual fund companies, asset owners, research firms, financial planners, advisors and broker-dealers, represent more than $3 trillion in assets under management or advisement. US SIF members integrate environmental, social, and governance factors into their investment decisions vote proxies and engage with companies. Our members' have brought multiple resolutions over the past three decades, bringing meaningful changes in company policies and practices.

The Release proposes two main categories of amendments to federal securities laws that regulate proxy advisory firms. The amendments would:

1. Codify that furnishing proxy voting recommendations, research and analysis is considered to be engaging in a proxy solicitation, requiring substantial information and filing requirements, and subject proxy advisors to Rule 14a-9 liability for materially misleading statements or omissions.

2. Establish new conditions or hurdles for proxy advisors, including requiring that they:
    a. disclose material conflicts of interest in a specified manner;
    b. provide an opportunity for companies and "other reviewing persons" to review and give feedback on the draft proxy advisor report;
    c. provide an additional opportunity for companies to review a "final" report; and
    d. allow companies to provide a written response to the report.

US SIF's members take seriously their obligation to vote shares in a thoughtful and informed manner, consistent with their fiduciary responsibilities to their investors. US SIF members have found proxy advisors to provide a high level of independent analysis on the myriad issues that must be voted on at the thousands of shareholder meetings that are held each year.

The Release would make it more difficult, expensive, or time-consuming for proxy advisors to provide that research. In fact, the amendments would stifle independent views and would not help institutional investors get better information and thus serve their clients better. Rather it weakens an important source of data.

Concerns raised in the proposed rule about possible bias on the proxy advisor's part is addressed by the current practice where proxy advisors make public and invite comment on their voting guidelines.

We submit that the need for regulatory action is, at best, unproven, and there are significant regulatory safeguards now in effect. In addition, the amendments will compromise the independence of the proxy advisor research and thus harm investor interests.

The Release is affirmatively harmful to investors and is thus contrary to the Commission's mandate to protect investors. It should be withdrawn.

<u>Background</u>

To provide context for our comments, it is important to note that proxy advisors came into being in response to a significant market failure – the asymmetric information that exists between a company and its shareholders. There was little that a shareholder could do about the lack of quality research, particularly if the investor-owned shares in a number of companies. The prevailing philosophy in those days was the "Wall Street Rule," *i.e.*, if a shareholder did not like what a company was doing, the shareholder should sell his or her stock.

By the 1980s, however, the situation had changed, as shareholders began to show a greater interest in understanding a range of issues affecting their portfolios. Some of these were environmental, social and governance issues raised in proposals filed by other shareholders. In addition, shareholders needed to understand executive compensation plans, director performance and other governance issues raised in management-placed voting items. The time required to research the issues and obtain company data would have been daunting for most investment management firms. Professional proxy advisors came along to fill the vacuum by providing the sort of independent analysis that investors would need as new issues came to the fore and needed to be addressed. Because they served multiple clients, they also could benefit from economies of scale and offer research and analysis at a lower cost than most of their clients would have realized had they attempted the same level of research in-house.

The current exemption from proxy solicitation for proxy advisors (Rule 14a-2(b)(3)) states that a proxy advisor must disclose to an investment advisor "any significant relationship with the registrant or any of its affiliates, or a security holder proponent of the matter on which advice is given, as well as any material interests of the advisor in such matter." In *Staff Legal Bulletin No. 20, Proxy Voting: Proxy Voting Responsibilities of Investment Advisers and Availability of Exemptions from the Proxy Rules for Proxy Advisory Firms* (2014), available at https://www.sec.gov/interps/legal/cfslb20.htm, the staff stated that a relationship could be viewed as "significant," or that a "material interest" could exist if knowledge of the relationship or interest could reasonably be expected to affect how a reader of the information might gauge the reliability and objectivity of the proxy advisor.

Moreover, US SIF members who act as investment advisors have fiduciary obligations to their investors. They have their own voting guidelines, and they do not – and cannot -- blindly follow proxy advisor recommendations. However, they do consider the views expressed by those advisors as one of many factors that enter into the decision-making process. Differently put, the clients of proxy advisors are licensed investment professionals who have their own fiduciary obligations to consider in assessing information provided by proxy advisors and any other sources. The Commission has spelled out those fiduciary obligations in Rule 206(4)-6 and reiterated the importance of those responsibilities recently in *Commission Guidance Regarding Proxy Voting Responsibilities of Investment Advisers*, Release No. IA-5325, IC-33605, 84 Fed. Reg. 47420 (Sept. 10, 2019).

What is the SEC trying to fix?

With this as our baseline, it is unclear what the SEC is trying to fix in its current release.

The Release posits two issues, the first of which is a need for enhanced disclosure about conflicts of interest on the proxy advisor's part. As stated above, US SIF believes the SEC currently has the authority to enforce conflict disclosure.

The second issue, inaccurate proxy advisor reports, is surprisingly short on specifics. The Release states the concern of business representatives that "there could be factual errors, incompleteness or methodological weaknesses" in proxy advisor reports and cites several letters to that effect in a footnote (84 Fed. Reg. at 66528 & n.94). However, the Release does not identify specific examples that, in the Commission's view, are the sorts of errors that the Release would cure. The Release does note that some allegedly factual errors may simply be differences of opinion. However, the Release does not state whether the Commission has analyzed the issue sufficiently to assess whether there really is a problem or whether these alleged errors are material to voting decisions -- or whether the proposed cure would solve the problem without diminishing the value of communications from independent advisors to investment advisors. The October 25, 2019 letter submitted by the Council of Institutional Investors (available at https://www.sec.gov/comments/4-725/4725-6357861-196392.pdf), confirms our view of a lack of pervasive errors in proxy advisor research.

US SIF is especially concerned by the Commission's defense of what we regard as an unnecessary review process and a heavy-handed requirement that proxy advisors include company responses in any reports. The Commission states that "providing the clients of proxy voting advice businesses with convenient access to the views of the registrant and certain other soliciting persons at the same time they receive the proxy voting advice could improve the overall mix of information available when the clients make their voting decisions" (84 Fed. Reg. at 66530).

US SIF believes that this depiction is backward. Company proxy statements lay out in considerable detail the facts of their operations and information about policies and recommendations on which they ask their stockholders to cast a "yes" vote. It is the proxy advisors who are enriching the dialogue by providing independent analysis of those policies and recommendations. If a company disagrees or has a methodological difference with how a proxy advisor addresses an issue, the company has the resources to respond without forcing a proxy advisor to carry a message (at the advisor's expense) with which it disagrees.

There also seems to be an inconsistency between the Commission's approach in this case and the approach in the companion rulemaking involving shareholder proposals. In the latter, the Commission starts from the premise that Rule 14a-8 needs to be tightened up because shareholder proposals are imposing a significant cost burden on companies required to print and mail those proposals. In this rulemaking, however, proxy advisors must be forced at their own expense to print company objections with which the advisor agrees, regardless of the cost.

If anything, we believe that the Release would stifle independent views, particularly on the topic of executive compensation, where self-interest may come into play. As SEC Commissioner Jackson pointed out in his statement opposing adoption of the Release, a proxy advisor will have to prepare a draft report and provide it to management, which will inevitably disagree with any negative views expressed on compensation issues. The advisor must then decide how to respond, and if management disagrees with the proxy advisor's final report, the proxy advisor must include management's views in the advisor's report. Given that disagreements can lead to complaints that a proxy advisor is violating federal securities law, it is difficult to imagine a process more designed to chill the proxy advisor's speech.

We believe the proposed rule is so heavy-handed that it would unduly impose burdens not only on their proxy advisors but also on their clients without any benefits to investors.

Thank you for the opportunity to submit these comments.

Sincerely,

Lisa N. Woll

Lisa Woll
CEO